Flash Economics

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The risk of crisis entailed by the Trump administration's policies

The Trump administration is pursuing an economic policy that includes:

- A reduction in the capital requirements for major banks (by 1.5 percentage points of risk-weighted assets);
- A substantial cut in short-term interest rates, probably following the replacement of Jerome Powell as Chair of the Federal Reserve;
- A very high public deficit (exceeding 7% of GDP from the 2025–2026 fiscal year onwards), despite a very low unemployment rate;
- Tariffs that are 15 percentage points higher than they were at the beginning of 2025;
- Support for the development of cryptocurrencies and stablecoins.

One can imagine a chain of events leading to a financial crisis:

- Depreciation of the dollar (due to a more expansionary monetary policy);
- Rising inflation and falling growth (as a result of tariffs and expansionary fiscal policy at full employment);
- A decline in foreign demand for dollar-denominated assets (bonds and equities) due to lower returns for non-residents;
- Tumbling stock market indices and an increasingly difficult financing of the public deficit;
- Losses for banks, while being less well-capitalised (due to falling share prices and slower growth), and for stablecoin issuers (due to the decline in the value of the securities held as collateral for issued stablecoins);

  Resulting in a global financial crisis (involving balance of payments, stock markets, public debt, and financial institutions).

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Five major economic policy decisions taken by the Trump administration

The Trump administration has taken **five economic policy decisions that risk plunging the United States into an economic and financial crisis**:

1. **The reduction of capital requirements for major banks** – likely by 1.5 percentage points of banks' risk-weighted assets.
2. **The replacement of Jerome Powell at the end of his term as Chair of the Federal Reserve**, very likely by someone far more supportive of lower interest rates.
3. **A very high public deficit** (exceeding 7% of GDP) from the 2025–2026 fiscal year onwards, given the significant tax cuts planned in the "Big Beautiful Bill", despite the unemployment rate being very low.
4. **Tariffs on all U.S. imports**, currently 15 percentage points higher than they were at the start of 2025.
5. **Support for the development of cryptocurrencies and stablecoins**.

The chain reaction through which these economic policy decisions could trigger an economic and financial crisis

1. Depreciation of the dollar

The expectation of a more expansionary monetary policy in the United States—driven by cuts in short-term interest rates—has already led to a **depreciation of the dollar** since the beginning of 2025 (Charts 1a/b), a trend that is expected to intensify in the future.

Chart 1A
Euro/dollar exchange rate (EUR 1 = USD...)

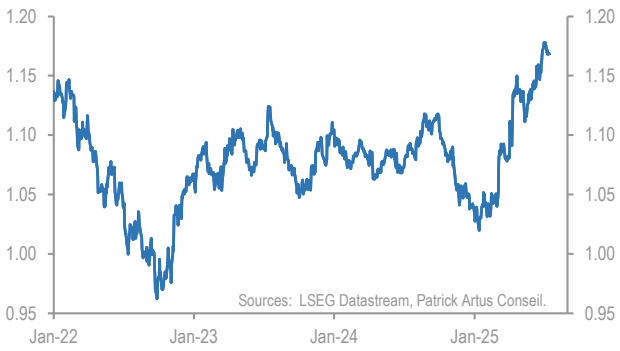
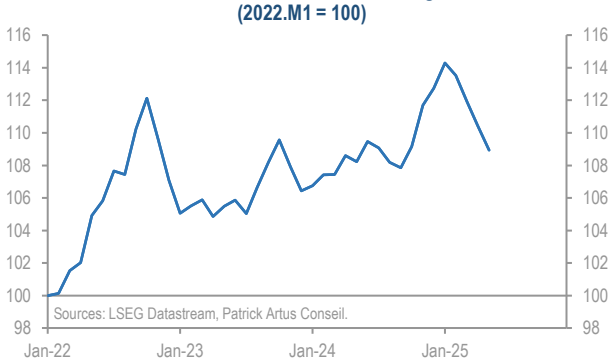


Chart 1B
United States: Real effective exchange rate (2022.M1 = 100)



2. Rising inflation and slowing growth

The increase in tariffs and the expansionary monetary policy implemented while the economy is at full employment will lead **to a rise in core inflation** (**Chart 2**). As wages in the United States are only weakly indexed to inflation, this will result in **a decline in purchasing power, a reduction in household consumption** (**Chart 3**), **and ultimately slower economic growth**.

Chart 2
United States: Core inflation
(CPI excl. food and energy, Y/Y as %)

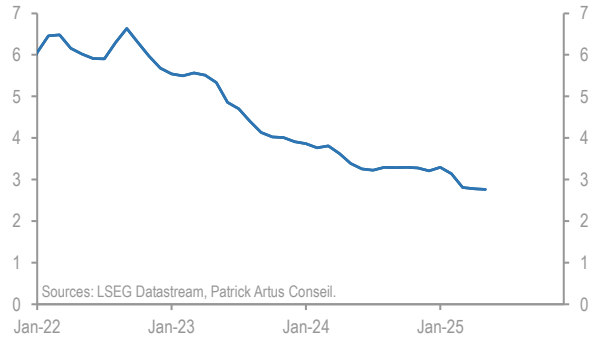
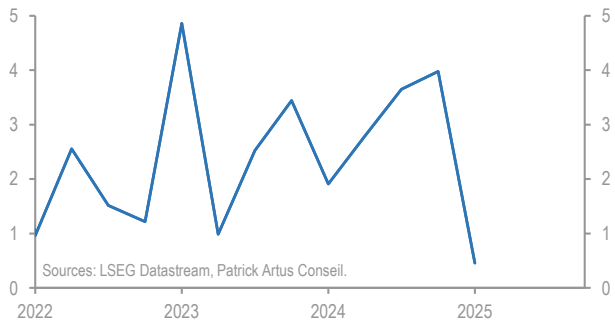


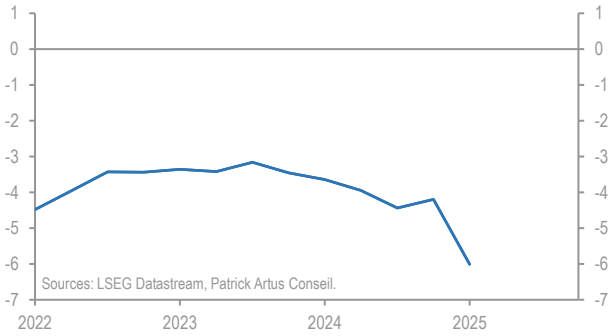
Chart 3
United States : Household consumption
(in volume terms, Q/Q as % annualised)



3. Decline in foreign demand for dollar-denominated assets

Foreign demand for dollar-denominated assets (bonds, equities, and business shares) is expected to fall, due to the anticipated depreciation of the dollar and to weakening economic growth. These two developments will reduce the return on dollar assets for non-residents. As a result, **the United States will face increasing difficulties in financing its current account deficit** (**Chart 4**).

Chart 4
United States: Current account balance
(as % of nominal GDP)



4. Falling stock market indices and difficulty financing the public deficit

As foreign demand for dollar-denominated assets declines, stock market indices will fall (**Chart 5**), and it will become more difficult to finance the **public deficit** (**Chart 6**). This will lead to a rise in long-term interest rates (**Chart 7**).

Chart 5
United States: Stock market indices (01.01.2022 = 100)

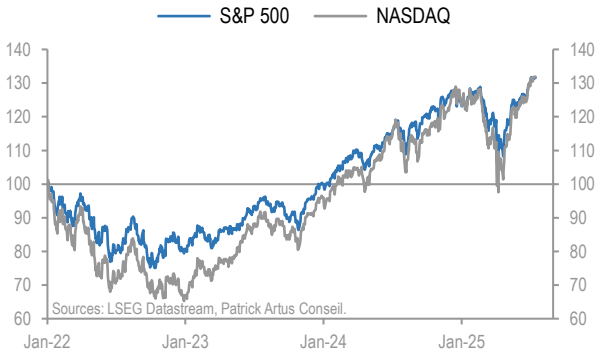


Chart 6
United States: Budget deficit (as % of nominal GDP)

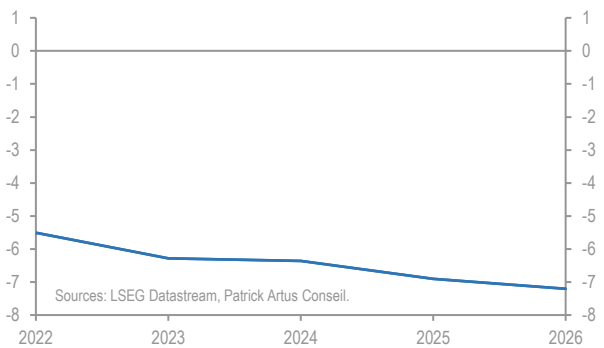
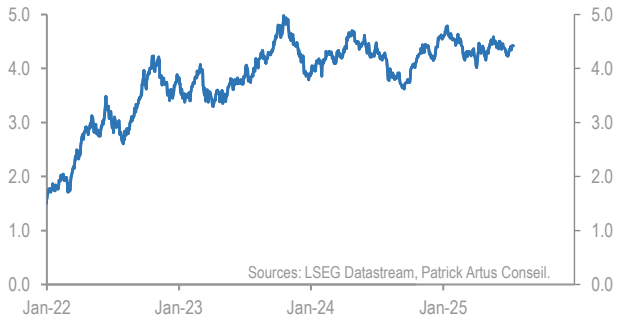


Chart 7
United States: Interest rate on 10-year government bonds
(as %)



5. Difficulties for banks and stablecoin issuers

The decline in stock market indices and slowing growth will generate **losses for U.S. banks**—particularly concerning given that deregulation will have allowed them to lower their capital buffers. The fall in the value of U.S. Treasuries held by **stablecoin issuers** as collateral for the funds they collect would lead to losses and could potentially trigger a run on these issuers.

Summary: the risk of a comprehensive economic and financial crisis for the United States

The economic policy decisions of the Trump administration expose the United States to the risk of a comprehensive economic and financial crisis:

- **A balance of payments crisis**, due to insufficient capital inflows to finance the current account deficit;
- **A public debt crisis**, driven by declining purchases by non-residents;
- **A financial institutions crisis**, (affecting banks, due to falling stock indices and lower growth, and stablecoin issuers, due to the declining value of their Treasury holdings).

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